

## Union Pacific(UNP)

**\$174.41** (As of 07/28/20)

Price Target (6-12 Months): **\$185.00**

Long Term: 6-12 Months

**Zacks Recommendation:**
**Neutral**

(Since: 03/26/19)

Prior Recommendation: Outperform

Short Term: 1-3 Months

**Zacks Rank:** (1-5)

**3-Hold**

Zacks Style Scores:

VGM:B

Value: B

Growth: C

Momentum: A

### Summary

Union Pacific is suffering a dismal freight revenue scenario (down 14% in first-half 2020). Freight revenues are being hurt, mainly by coronavirus-induced depressed volumes (down 13% in first-half 2020). Weakness in the Bulk, Premium and Industrial units weighed on the overall volume picture. Overall volumes are likely to decline around 10% in the current year. Deterioration in the debt-to-EBITDA ratio is an added woe. However, efforts to control costs, courtesy of the precision scheduled railroading model, are a positive, particularly, in the wake of revenue concerns. Mainly owing to cost-cutting efforts, operating ratio is predicted to improve in 2020. The company's ability to generate free cash flow (up 58.9% in first-half 2020) is also a boon. Further, the uptick in e-commerce demand during the pandemic is encouraging.

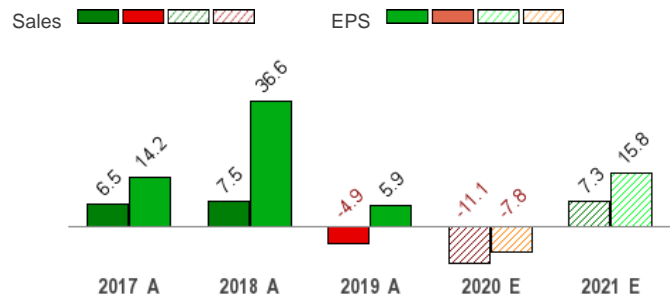
### Price, Consensus & Surprise



### Data Overview

52 Week High-Low	\$188.96 - \$105.08
20 Day Average Volume (sh)	2,807,248
Market Cap	\$118.4 B
YTD Price Change	-3.5%
Beta	1.06
Dividend / Div Yld	\$3.88 / 2.2%
Industry	<a href="#">Transportation - Rail</a>
Zacks Industry Rank	Bottom 30% (177 out of 253)

### Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	3.7%
Last Sales Surprise	-3.5%
EPS F1 Est- 4 week change	0.6%
Expected Report Date	10/15/2020
Earnings ESP	-1.5%
P/E TTM	21.6
P/E F1	22.6
PEG F1	2.3
P/S TTM	5.9

### Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	5,132 E	5,252 E	5,276 E	5,268 E	20,720 E
2020	5,229 A	4,244 A	4,845 E	4,963 E	19,308 E
2019	5,384 A	5,596 A	5,516 A	5,212 A	21,708 A

### EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$2.11 E	\$2.28 E	\$2.32 E	\$2.33 E	\$8.95 E
2020	\$2.15 A	\$1.67 A	\$1.92 E	\$2.02 E	\$7.73 E
2019	\$1.93 A	\$2.22 A	\$2.22 A	\$2.02 A	\$8.38 A

\*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 07/28/2020. The reports text is as of 07/29/2020.

## Overview

Union Pacific Corporation provides rail transportation services across 23 states in the United States through its principal operating company, Union Pacific Railroad Company. As the largest railroad in North America, Union Pacific connects the Pacific and Gulf Coast ports with the Midwest and gateways in eastern United States.

The company also connects with Canada's rail systems and is the only railroad, serving all the six major gateways to Mexico. Union Pacific offers transportation services for agricultural products, automotive, lumber, steel, paper, food, chemicals, coal, and industrial products, as well as for finished vehicles and intermodal containers.

Union Pacific, based in Omaha, NE, also provides container and traffic services, primarily for shipper agents and consolidators, as well as for truckload carriers. The company was incorporated in Utah in 1969.

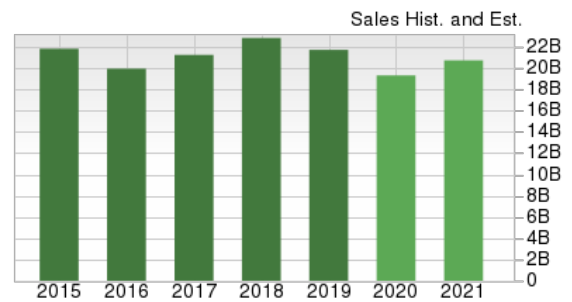
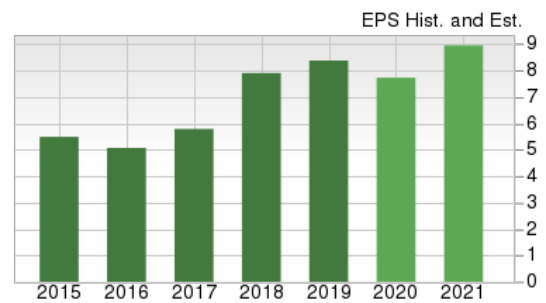
From first-quarter 2020, Union Pacific will report through three business groups: **Bulk** (formerly agricultural products), **Industrial** and **Premium**.

The bulk division (31.4% of freight revenues generated in 1Q20) is responsible for the transportation of grains, commodities produced from these grains, fertilizer apart from food and beverage products. The segment serves major grain markets, linking the Midwest and Western United States producing areas to export terminals in the Pacific Northwest and Gulf Coast ports and Mexico. The coal and petroleum coke products also come under the bulk group.

The Industrial unit (38.8%) includes multiple categories like construction, industrial chemicals and soda ash. The company's premium division includes three segments, namely international intermodal, domestic intermodal and finished vehicles. Meanwhile, LPG, petroleum and sand products also fall under its Industrial business.

The company's premium division (29.8%) includes three segments, namely international intermodal, domestic intermodal and automotive. Freight revenues account for bulk of the company's top line. In the first quarter of 2020, 93.3% of the company's total revenues of \$5,229 million came from this source.

The company's fiscal year coincides with the calendar year.



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## Reasons To Buy:

- ▲ We are encouraged by the company's efforts to check costs in a bid to drive the bottom line. Operating expenses contracted 16% to \$5,676 million in first-half 2020. Increased efficiency from the precision scheduled railroading model is likely to have contained costs. Mainly owing to cost-cutting efforts, operating ratio is predicted to improve in 2020.
- ▲ We are also pleased by the efforts of the company to promote safety and enhance productivity. To this end, the company completed the implementation of positive train control (PTC) on its network in December 2019. The technology is now implemented on Union Pacific's entire federally mandated rail lines, including required passenger train routes. Notably, the company generated productivity savings worth \$590 million in 2019. Productivity savings in excess of \$500 million are expected in 2020. In first-half 2020, employee safety results improved 5%.
- ▲ In this coronavirus-ravaged world, e-commerce — the method of buying and selling goods and services via a software platform — is gaining further momentum. This is because the need for door-to-door delivery of essentials during this unprecedented crisis is rising. E-commerce, which already became part and parcel of daily lives in today's fast-paced times, is witnessing higher demand now amid the pandemic-induced social-distancing protocols, quarantine and lockdowns. The surge in e-commerce boosted Union Pacific's parcel business. On a separate note, we are also bullish on its ability to generate free cash flow (\$1,656 million in the first half of 2020, up 58.9% year over year).

We are pleased by the company's efforts toward promoting safety and enhancing productivity.

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### Reasons To Sell:

- ▼ Union Pacific is suffering a dismal freight revenue scenario (down 14% in first-half 2020). Freight revenues are being hurt, mainly by coronavirus-induced depressed volumes (down 13% in first-half 2020). Weakness in the Bulk (volumes down 15% in first-half 2020), Premium (down 23%) and Industrial (down 18%) units weighed on the overall volume picture. Overall volumes are down 7% for the September quarter as of Jul 21, 2020. Overall volumes are anticipated to decline around 10% in the current year.
- ▼ We are concerned about Union Pacific's high-debt levels. Debt/EBITDA ratio (adjusted) at Union Pacific deteriorated to 2.3 in 2018 from 1.9 in 2017. It increased to 2.5 at the end of 2019. The measure has increased further to 2.9 at the end of the first six months of 2020. A high debt/EBITDA ratio often indicates that a firm may be unable to service its debt appropriately.
- ▼ We are concerned about the year-over-year decrease in the top line in second-quarter 2020 due to weakness in freight revenues. Apart from declining volumes, weakness pertaining to average revenue per car is dragging down freight revenues. The top line is likely to take a hit in the remaining quarters of 2020 from lackluster freight revenues (which account for bulk of the top line).

Union Pacific suffers from dismal freight revenues mainly due to volume woes.

## Last Earnings Report

### Earnings Beat at Union Pacific in Q2

Union Pacific's earnings of \$1.67 per share surpassed the Zacks Consensus Estimate of \$1.61. However, the bottom line declined 24.8% on a year-over-year basis. Operating revenues of \$4,244 million missed the Zacks Consensus Estimate of \$4,399.3 million. The top line also declined 24.2% on a year-over-year basis due to sluggish freight revenues (down 24%). Business volumes, measured by total revenue carloads, declined 20% year over year.

Operating income in the second quarter declined 27% year over year to \$1,654 million. Operating expenses contracted 22% to \$2,590 million. As a result, operating ratio (operating expenses as a percentage of revenues) deteriorated to 61% from 59.6% in the year-ago quarter due to weak shipments.

Moreover, the company's second-quarter effective tax rate came in at 24.3% compared with 23.7% in the year-ago quarter. Total capital expenses were \$1,599 million in the second quarter.

### Segmental Performance

Bulk (Grain & grain products, Fertilizer, Food & refrigerated, Coal & renewables) freight revenues were \$1,386 million, down 17% year over year. Revenue carloads too slid 15%. Moreover, average revenue per car fell 3% year over year.

Industrial freight revenues totaled \$1,500 million, down 23% year over year. Also, revenue carloads fell 18% and average revenue per car fell 6% on a year-over-year basis.

Freight revenues in the Premium division were \$1,086 million, down 33% year over year. Moreover, revenue carloads dropped 23% year over year. Moreover, average revenue per car declined 13%.

Meanwhile, other revenues slipped 24% to \$272 million in the second quarter.

### Liquidity

The company exited the June end quarter with cash and cash equivalents of \$2,706 million compared with \$831 million at the end of 2019. Debt (due after a year) amounted to \$26,439 million at the end of the quarter from \$23,943 million at 2019-end. Debt-to-EBITDA ratio (on an adjusted basis) deteriorated to 2.9 from 2.5 at 2019-end.

### 2020 Outlook

Owing to the COVID-19 led uncertainty looming in the economy, Union Pacific expects its full year 2020 carload volumes to be approximately around 10% compared with 2019 levels.

Quarter Ending **06/2020**

Report Date	Jul 23, 2020
Sales Surprise	-3.53%
EPS Surprise	3.73%
Quarterly EPS	1.67
Annual EPS (TTM)	8.06

## Valuation

Union Pacific shares are down 3.5% year to date and 2.7% over the past year. Stocks in the Zacks sub-industry are up 0.9% and those in the Zacks Transportation sector are down 8.4% on a year-to-date basis, respectively. Over the past year, the Zacks sub-industry is up 2.2% and the sector is down 7.8% .

The S&P 500 index is up 0.9% year to date and 8% over the past year.

The stock is currently trading at 20.66X forward 12-month price-to-earnings, which compares to 19.05X for the Zacks sub-industry, 35.05X for the Zacks sector and 22.61X for the S&P 500 index.

Over the past five years, the stock has traded as high as 23.59X and as low as 11.77X, with a 5-year median of 17.64X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$185 price target reflects 21.91X forward 12-month earnings.

The table below shows summary valuation data for UNP

Valuation Multiples - UNP					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	20.66	19.05	35.05	22.61
	5-Year High	23.59	19.35	36.06	22.61
	5-Year Low	11.77	13.46	10.48	15.25
	5-Year Median	17.64	16.8	13.35	17.52
EV/EBITDA TTM	Current	13.38	13.93	7.62	12.04
	5-Year High	32.29	31.25	11.21	12.85
	5-Year Low	7.11	7.86	5.45	8.25
	5-Year Median	11.72	12.21	7.39	10.88
P/S F 12M	Current	5.76	5.72	1.3	3.57
	5-Year High	6.19	5.72	1.42	3.57
	5-Year Low	2.7	3.04	0.85	2.53
	5-Year Median	4.44	4.55	1.2	3.02

As of 07/28/2020

## Industry Analysis Zacks Industry Rank: Bottom 30% (177 out of 253)



## Top Peers

Company (Ticker)	Rec	Rank
Canadian National Railway Company (CNI)	Outperform	1
Canadian Pacific Railway Limited (CP)	Outperform	2
Caterpillar Inc. (CAT)	Neutral	3
CSX Corporation (CSX)	Neutral	3
FedEx Corporation (FDX)	Neutral	3
Kansas City Southern (KSU)	Neutral	3
Norfolk Southern Corporation (NSC)	Neutral	4
United Parcel Service, Inc. (UPS)	Neutral	3

Industry Comparison Industry: Transportation - Rail				Industry Peers		
	UNP	X Industry	S&P 500	CSX	KSU	NSC
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	3	3	4
VGM Score	B	-	-	B	C	B
Market Cap	118.40 B	20.29 B	22.47 B	53.66 B	14.61 B	51.18 B
# of Analysts	10	7	14	10	8	10
Dividend Yield	2.22%	1.71%	1.84%	1.48%	1.03%	2.03%
Value Score	B	-	-	B	B	C
Cash/Price	0.02	0.05	0.07	0.05	0.04	0.01
EV/EBITDA	12.90	12.16	13.04	10.50	14.20	11.92
PEG Ratio	2.26	2.65	2.97	2.62	1.54	3.29
Price/Book (P/B)	7.20	3.44	3.11	4.41	3.08	3.44
Price/Cash Flow (P/CF)	14.88	12.40	12.07	11.72	14.33	12.40
P/E (F1)	22.56	22.56	21.52	19.95	23.05	21.46
Price/Sales (P/S)	5.86	4.76	2.35	4.89	5.30	4.62
Earnings Yield	4.43%	4.39%	4.34%	5.01%	4.34%	4.66%
Debt/Equity	1.61	0.79	0.76	1.33	0.81	0.79
Cash Flow (\$/share)	11.72	6.11	7.01	5.98	10.81	14.93
Growth Score	C	-	-	D	C	C
Hist. EPS Growth (3-5 yrs)	13.50%	12.62%	10.85%	23.81%	11.73%	18.67%
Proj. EPS Growth (F1/F0)	-7.74%	-12.14%	-7.56%	-15.73%	-2.61%	-16.58%
Curr. Cash Flow Growth	-0.27%	1.21%	5.47%	0.86%	8.60%	3.26%
Hist. Cash Flow Growth (3-5 yrs)	2.78%	5.61%	8.55%	8.74%	5.61%	5.66%
Current Ratio	0.96	1.03	1.31	1.62	2.44	0.90
Debt/Capital	61.64%	44.59%	44.41%	57.01%	44.59%	44.24%
Net Margin	27.54%	21.74%	10.44%	26.39%	20.63%	21.89%
Return on Equity	32.45%	16.49%	15.10%	24.24%	13.80%	18.12%
Sales/Assets	0.32	0.32	0.54	0.28	0.28	0.30
Proj. Sales Growth (F1/F0)	-11.06%	-8.54%	-1.97%	-12.15%	-7.31%	-13.35%
Momentum Score	A	-	-	B	F	B
Daily Price Chg	-1.36%	-1.20%	-0.80%	-2.08%	-1.04%	-2.54%
1 Week Price Chg	-2.83%	-0.90%	0.37%	-1.14%	-3.49%	-0.66%
4 Week Price Chg	3.16%	3.73%	3.64%	0.52%	3.73%	5.43%
12 Week Price Chg	11.53%	9.93%	11.56%	9.93%	23.49%	8.02%
52 Week Price Chg	-2.73%	-2.73%	-3.92%	-0.16%	24.15%	-3.85%
20 Day Average Volume	2,807,248	245,277	1,867,919	3,231,041	867,237	1,329,002
(F1) EPS Est 1 week change	0.04%	0.00%	0.00%	-0.82%	0.00%	-0.77%
(F1) EPS Est 4 week change	0.64%	0.00%	0.21%	-1.54%	-0.28%	-1.91%
(F1) EPS Est 12 week change	-2.25%	-4.53%	-1.29%	-5.10%	-3.95%	-9.09%
(Q1) EPS Est Mthly Chg	-0.13%	1.24%	0.09%	2.04%	-1.07%	0.55%

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## Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

### Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

### Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

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### Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	<b>B</b>
Growth Score	<b>C</b>
Momentum Score	<b>A</b>
VGM Score	<b>B</b>

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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